STATE OF UTAH INSURANCE DEPARTMENT

REPORT OF FINANCIAL EXAMINATION

of

MOLINA HEALTHCARE OF UTAH, INC.
dba American Family Care of Utah, Inc.

of

Midvale, Utah

as of

December 31, 2001

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November 20, 2002

Honorable Merwin U. Stewart
Insurance Commissioner
State of Utah
3110 State Office Building
Salt Lake City, UT 84114

Commissioner:

Pursuant to your instructions and in compliance with statutory requirements, an examination, as of December 31, 2001, has been made of the financial condition and business affairs of:

MOLINA HEALTHCARE OF UTAH, INC.
dba American Family Care of Utah, Inc.
Midvale, Utah

hereinafter referred to in this report as the Organization, and the following report of examination is respectfully submitted.

SCOPE OF EXAMINATION

Period Covered by Examination

The current examination covers the period from January 1, 1998, through December 31, 2001, including any material transactions and/or events occurring subsequent to the examination date noted during the course of the examination.

Certificates of representation attesting to the Organization's ownership of all assets and to the nonexistence of unrecorded liabilities were signed by and received from the Organization's management at the initiation and conclusion of the examination.

Examination Procedure Employed

The examination included a general review and analysis of the Organization's operations, the manner in which its business was conducted, and a determination of its financial condition as of December 31, 2001. The examination was conducted in accordance with generally accepted standards and procedures of regulatory authorities relating to such examinations.

Status of Prior Examination Findings

The previous examination was performed by the Utah Insurance Department as of December 31, 1997. Items of significance noted in the prior examination report summary

were corrected both during the prior examination and during the current examination period.

HISTORY

General

The Organization was incorporated under the laws of the State of Utah on May 27, 1994, as a wholly owned subsidiary of Molina Medical Centers. On May 1, 1996, the Utah Insurance Department issued the Organization a Certificate of Authority to conduct business as a health maintenance organization (HMO).

Effective January 1, 2000, 100% of the Organization's stock was transferred from Molina Medical Centers to American Family Care, Inc., a holding company now known as Molina Healthcare, Inc. The ownership of Molina Healthcare, Inc. was identical to the prior ownership of Molina Medical Centers, therefore, no change of control took place as a result of the reorganization. The Organization amended its articles of incorporation on February 25, 2000, and the name of the corporation was changed from American Family Care of Utah, Inc. to Molina Healthcare of Utah, Inc.

The Organization's bylaws, articles of incorporation and minutes of the board of directors meetings and sole shareholder meetings held during the period covered by this examination were reviewed. The Organization amended Article I of its articles of incorporation on February 25, 2000, to change its name to Molina Healthcare of Utah, Inc. In addition, Articles II, III, IV, IX and X were amended. Article II stated "The Corporation shall operate as a health maintenance organization, subject to licensure pursuant to Chapter 8 of the Utah Insurance Code, and shall engage in business reasonably incidental thereto." The word "purpose" was replaced in Article III with the word "powers" in reference to the powers of the Corporation. The following language was added to Article IV in reference to the one hundred thousand shares of $1.00 par value common stock: "Said shares shall have unlimited voting rights. Upon dissolution of the Corporation, the holders of said shares are entitled to receive the net assets of the Corporation." Article IX amended the list of current principal officers of the Corporation, and Article X was amended to state the current address of the Corporation's principal place of business.

Capital Stock

As of December 31, 2001, the number of shares of common stock authorized by the Company was 100,000 at a par value of $1.00 each. The number of shares issued and outstanding was 100,000. Molina Healthcare, Inc. owned 100% of the outstanding shares of common stock.

Dividends to Stockholders

The Organization made an extraordinary dividend distribution of $500,000 to its parent in the last quarter of 1999. The Organization did not comply with Utah Code Annotated (U.C.A.) § 31A-16-106(2)(a), which requires a 30-day prior notification to the Commissioner. The Organization filed a Form D Prior Notice of a Transaction with the Commissioner on July 31, 2000. The extraordinary dividend was approved.

Management

The bylaws of the Organization indicated the number of directors may be fixed or changed from time to time with the initial number of five (5). "The number of directors composing the Board of Directors shall never be less than three… Inside directors, as defined in Section 31A-5-407(3) of the Utah Insurance Code, may not constitute a majority of the Board."

The following persons served as directors of the Organization as of December 31, 2001:

Name	Principal Occupation
Joseph M. Molina M.D. Long Beach, California	Chief Executive Officer Molina Healthcare, Inc.
George S. Goldstein, P.H.D. Long Beach, California	Chief Executive Officer Molina Healthcare of California
George Kirk Olsen Sandy, Utah	President/Chief Executive Officer Molina Healthcare of Utah, Inc.
Clayton S. Wilde, M.D. Salt Lake City, Utah	Physician
Suzanne C. Ferry Corinne, Utah	Legislative Executive Consultant
Lorin C. Barker Salt Lake City, Utah	Attorney at Law Kirton & McConkie
Charles A. Coonradt Park City, Utah	President/Owner The Game of Work, Inc.

The Company's bylaws provide for principal officers to consist of a "President, a Vice President and a Secretary/Treasurer." The directors as may be deemed necessary may appoint other officers. "The same individual may simultaneously hold more than

one office in the Corporation, except that the principal officers of the Corporation must be separate natural persons."

The officers of the Organization as of December 31, 2001, were as follows:

Principal Officer	Office
George Kirk Olsen	President/Chief Executive Officer
John C. Molina, J.D.	Vice President
Mark L. Andrews	Secretary
Paul J. Muench	Treasurer

The Organization was not in compliance with U.C.A. § 31A-5-410(1)(a). The Commissioner was not notified immediately after the election of one director and two principal officers during the examination period. Biographical affidavits were not filed with the Utah Insurance Department for George S. Goldstein, Mark L. Andrews, and Paul J. Muench.

The members of the Organization's audit committee as of December 31, 2001, were as follows:

Audit Committee Members
Lorin C. Barker
Charles A. Coonradt
Suzanne C. Ferry
Clayton S. Wilde, M.D.

The minutes of the meetings of the credentialing committee and quality improvement committee were reviewed for examination purposes. The minutes of the meetings of the board of directors did not include a resolution to appoint members of the two committees as required by Article II Section G of the Organization's bylaws.

Conflict of Interest Procedure

According to Section I of the bylaws, 'The Board of directors shall require officers and directors of the Corporation to complete annual disclosure statements regarding conflicts of interest and "party-in-interest" transactions.' No disclosure statements were completed during the examination period ending December 31, 2001. During the course of the examination, all of the board members completed disclosure statements, and the officers, except John C. Molina, completed disclosure statements.

Corporate Records

"The board shall manage the business and affairs of the corporation" in accordance with U.C.A. § 31A-5-407(6), however, the board minutes did not include the approval of investments.

The last meeting of the board of directors was held on October 5, 2001, and the board approved the minutes of that meeting on November 30, 2001. The Utah Insurance Department examination report as of December 31, 1997, dated March 4, 1999, was distributed to the board in May 1999.

AFFILIATED COMPANIES

The Organization is wholly owned and controlled by Molina Healthcare, Inc. An organizational chart illustrating the holding company system follows:

Transactions with Affiliates

Effective March 1, 2000, the Organization entered into a Services Agreement with Molina Healthcare, Inc. pursuant to which the parent provides services relative to (a) human resources, including consultation, administration and payroll, (b) information systems, including problem resolution, server service and information systems, (c) accounts payable, (d) legal advice, (e) financial consulting, (f) claims consulting, (g) medical consulting, and (h) strategic management consulting. The Organization did not file a Form D Prior Notice of a Transaction with the Commissioner 30 days in advance of the transaction pursuant to U.C.A. § 31A-16-106(1)(b)(iv).

Effective January 1, 2001, pursuant to the Services Agreement by and between the Organization and Molina Advantage, Inc., an affiliate operating as a third party administrator, the Organization provides personnel, information systems and management services to Molina Advantage, Inc.

RxAmerica provides management and administrative services for prescription drug benefit plans to the Organization under an agreement by and between RxAmerica and the Organization's affiliate, Molina Advantage, Inc. effective November 1, 1999. Molina Advantage, Inc. acts as an intermediary and agent for the Organization.

The Organization files a consolidated federal income tax return with its parent, Molina Healthcare, Inc. The parent collects the amount of taxes or benefits determined as if the subsidiary filed a separate return.

FIDELITY BOND AND OTHER INSURANCE

The Organization was a named insured on a joint endorsement attached to the fidelity bond policy of its parent, Molina Healthcare, Inc. The minimum fidelity coverage suggested by the National Association of Insurance Commissioners (NAIC) for an HMO of the Organization's size and premium volume is not less than $1,000,000. As of the examination date, the Organization participated in fidelity bond coverage of $2,000,000. The Organization also had additional insurance protection against loss from business personal property and liability risks.

PENSION, STOCK OWNERSHIP AND INSURANCE PLANS

As of the examination date, the Organization's eligible employees participated in a 401(k) plan, which allowed for contributions up to 14% of their pay with the Organization matching up to 4%. The Organization provided medical, dental, vision, short term disability and life insurance to its eligible employees and their dependents. Also, a deferred compensation plan was provided to management and key personnel.

STATUTORY DEPOSITS

The Organization's statutory deposit requirement was $550,000 pursuant to U.C.A. § 31A-8-211(1). The examination confirmed the Organization maintained a statutory deposit consisting of one U.S. Treasury Note with a market value of $574,892 and a par value of $575,000, which was adequate to cover the required deposit of $550,000.

INSURANCE PRODUCTS AND RELATED PRACTICES

Policy Forms and Underwriting

The Organization provided two lines of coverage, Medicaid and Children's Health Insurance Plan (CHIP). As of December 31, 2001, the Organization maintained an agreement with the State of Utah Department of Health (the State) to provide services under the Medicaid State plan in accordance with federal regulations governing Medicaid pre-paid managed care plans excluding dental and mental health services, which are provided by the State. It also maintained an agreement with the State to provide services under the CHIP State plan. The State performed underwriting and set premium rates based on negotiations with the Organization. The Organization was paid on a per member per month (PMPM) basis.

The Organization's member handbook was reviewed for compliance with Utah insurance laws, and no exceptions were noted. The Organization assumed the underwriting risk for "Covered Services." When the service is not covered, the Organization may bill an enrollee upon certain conditions. The Organization's risk retention limit was $50,000 and 20% of the costs exceeding $50,000, under provisions contained in the agreements with the State.

Territory and Plan of Operation

As of December 31, 2001, the Organization operated only in the State of Utah. The service area for the Medicaid plan was limited to the urban and rural counties of Cache, Davis, Iron, Salt Lake, Utah, Washington, and Weber. The CHIP managed care plan operated generally in the four urban counties along the Wasatch Front: Davis, Salt Lake, Utah, and Weber.

The Organization's marketing system was limited to enrollees qualified under the Medicaid and CHIP programs.

Advertising and Sales Material

The Organization marketed its programs to general population enrollees through advertising and direct marketing contacts with employers. The State was provided with brochures to distribute to potential enrollees.

Treatment of Policyholders

The Organization had a written complaint and grievance procedure in place to maintain control over policyholder complaints. There were no formal grievances filed with the Utah Insurance Department during the examination period.

Provider Contracts

The Organization contracted with approximately 2,000 providers to provide physician and ancillary services to its enrollees. A majority of these providers were located within the Wasatch Front metropolitan area. The Organization's provider contracts provide for payment on a Fee-For-Service (FFS) basis at a percentage ranging between 100% and 115% of the Utah Medicaid Fee Schedule with the exception of one contracted provider, which received a monthly capitation payment. Ancillary providers were paid a PMPM capitation amount, which had a risk corridor, and if the actual amount was greater or less than 10%, an adjustment was made.

In addition, one provider contract contained a hospital/outpatient surgery cost incentive pool. Under the Medicaid Incentive Pool, for any amount under 37.5% of the total applicable premium, the physician will be paid 40% [not to exceed 24% of the physician's total compensation] of the difference between the actual amount and 37.5% of the total applicable premium. Under the CHIP Incentive Pool, for any amount under 21% of the total applicable premium, the physician will be paid 40% [not to exceed 24% of the physician's total compensation] of the difference between the actual amount and 21% of the total applicable premium.

The following table lists compensation by provider type:

Provider Type	Medicaid Compensation Percentage of Utah Medicaid Fee Schedule	CHIP Compensation Percentage of Utah Medicaid Fee Schedule
Urban Primary Care	110%	110%
Urban Specialty Care	100%	100%
Urban Anesthesia	105%	105%
Rural Primary Care	115%	Not Applicable
Rural Specialist Fee-For-Service	112%	Not Applicable

The following table lists compensation for ancillary services:

Plan	Risk Corridor Measurement	Family Assistance Program	Total PMPM
CHIP A	$2.77	$1.92	$4.69
CHIP B	$1.92	$1.92	$3.84

Some provider agreements were not in compliance with U.C.A. § 31A-8-407(1), because the provider agreements did not contain the provision that the enrollee shall not be held liable to the provider for any sums owed by the Organization in the event the Organization fails to pay for health care services as set forth in the provider agreement.

REINSURANCE

The Organization's risk retention limit was $50,000 and 20% of the costs exceeding $50,000, under provisions contained in the agreements with the State during the beginning of the examination period for the year 1998, the first six months of 1999 and at the end of the examination period for the last six months of 2001.

Transamerica Occidental Life (Transamerica) provided reinsurance coverage for the policy period July 1, 1999 through June 30, 2000, and Centre Insurance Company (Centre) provided reinsurance coverage for the policy period July 1, 2000 through June 30, 2001. The Organization's risk retention for the earlier policy period was $50,000 and 20% of the costs exceeding $50,000. Its risk retention for the latter policy period was $50,000 and 10% of the costs exceeding $50,000. As of December 31, 2001, the Organization no longer maintained reinsurance contracts with Transamerica and Centre.

ACCOUNTS AND RECORDS

The Organization's accounting systems were maintained on a local area network. Subsidiary records were maintained in commercial software applications on stand-alone personal computers.

Data from these sources, along with the services of an independent accounting and consulting corporation, were used to prepare annual and quarterly statements, schedules and exhibits, and other financial statements. The same firm also maintained the general ledger.

The financial accounting functions were performed both at the Organizations' office in Midvale and at the Organization's parent office in Long Beach, California. The premium processing was centralized, collected, processed and accounted for in the Midvale office.

An independent certified public accounting firm audited the Organization's records during the period covered by this examination. Audit reports generated by the auditors for the years 1998 through 2000 were made available for the examiner's use.

The Organization's general ledger was maintained on an accrual basis. The examiner footed the Organization's general ledger trial balance and reconciled it to the balance sheet and income statement expenses and surplus contained in the December 31, 2001 annual statement. Individual financial statement accounts for the years covered in the examination period were reviewed and reconciled as deemed necessary.

Item nine of the general section of the *Annual Statement Instructions* promulgated by the NAIC states, "If the report does not contain the information asked for in the blanks or is not prepared in accordance with these instructions, it will not be considered filed." In addition, U.C.A. § 31A-2-202(6) requires that "All information submitted to the commissioner shall be accurate and complete."

Many of the annual statement reports, exhibits, and schedules were determined to be deficient or improperly prepared. Items of significance are listed below.

1. Number 1.3 of the 2001 General Interrogatories Part 1, reported the state regulating the Organization was California instead of Utah.

2. Note one of the 2001 Notes to Financial Statements stated the "DOI recognizes only statutory accounting practices prescribed or permitted by the state of Washington" instead of Utah.

3. The Organization did not complete the 1999 through 2001 Schedule E – Part 2 – Special Deposits contained in the annual statements.

4. The Organization's 2001 annual statement Schedule T – Premiums and Other Considerations did not reconcile to the Underwriting and Investment Exhibit – Part 1.

5. The Organization's 2001 annual statement Exhibit 3 – Accident and Health Premiums Due and Unpaid did not properly reflect the aging of premiums.

6. The 2001 Schedule Y – Part 2 Column 8 indicated the Organization paid $211,500 for management agreements and services contracts. This amount was paid for services provided by its parent, Molina Healthcare Inc. The Organization also had a service agreement with its affiliate, Molina Advantage, Inc. to provide personnel, information services and management services. The reporting line for Molina Healthcare of Utah, Inc. did not indicate the amount received from Molina Advantage, Inc.

7. Short-term investments of $4,608,976, were reported as cash. These investments should be reported on Schedule DA – Part 1, instead of Schedule E – Part 1 to be consistent with the NAIC *Annual Statement Instructions* and Part 11 Section 2 (a) of *the Purposes and Procedures Manual of the Securities Valuation Office (SVO)*.

8. Number 26 of the 2000 General Interrogatories stated the HMO's prior year's annual statement was not amended, however, the Organization amended its 1999 annual statement electronically with the NAIC and reported on the jurat page it was an original filing. The first amendment to the 2000 annual statement was also filed electronically with the NAIC, but neither amended annual statement was signed and executed and filed with the Commissioner in accordance with U.C.A. § 31A-4-113.

9. The minutes of the meetings held by the board of directors indicated the audit committee met prior to its meetings. The Organization stated in number 15 of the 2001 General Interrogatories the reporting entity kept a complete permanent record of the proceedings of its board of directors and all subordinate committees thereof. However, the audit committee did not maintain minutes of its meetings during the examination period.

FINANCIAL STATEMENTS

The following financial statements were prepared from the Organization's accounting records and the valuations and determination made during the examination:

BALANCE SHEET as of December 31, 2001

STATEMENT OF REVENUE AND EXPENSES for the Year Ended December 31, 2001

RECONCILIATION OF CAPITAL AND SURPLUS - 1998 through 2001

The accompanying NOTES TO FINANCIAL STATEMENTS are an integral part of the financial statements.

MOLINA HEALTHCARE OF UTAH, INC.
BALANCE SHEET
as of December 31, 2001

ASSETS

	Net Admitted Assets	Notes
Bonds	$ 574,892	
Cash and short-term investments	6,271,295	
Deferred compensation investment	12,148	
Accident and health premiums due and unpaid	1,208,888	(1)
Amounts recoverable from reinsurers	739,585	(2)
Amounts due from parent, subsidiaries and affiliates	202,168	(3)
Investment income due and accrued	9,523	
Federal and foreign income tax recoverable and interest thereon	955,474	(4)
Electronic data processing equipment and software	39,353	
Total assets	$ 10,013,326	

LIABILITIES, SURPLUS, AND OTHER FUNDS

Claims unpaid	$ 6,202,707	(6)
Unpaid claims adjustment expenses	190,512	(7)
General expenses due or accrued	262,927	(8)
Amounts due to parent, subsidiaries and affiliates	40,973	(9)
Total liabilities	6,697,119	
Common capital stock	100,000	
Gross paid in and contributed surplus	4,998,584	
Unassigned funds (surplus)	(1,782,377)	(10)
Total capital and surplus	3,316,207	
Total liabilities, capital and surplus	$ 10,013,326	

MOLINA HEALTHCARE OF UTAH, INC.
STATEMENT OF REVENUE AND EXPENSES
for the Year Ended December 31, 2001

	Total	Notes
Net premium income	$ 27,051,177	(1)
Total revenues	27,051,177	
Medical and Hospital:		
Hospital/medical benefits	22,144,202	
Outside referrals	4,876,971	
Other medical and hospital	432,413	
Subtotal	27,453,586	
Less:		
Net reinsurance recoveries	718,643	
Total medical and hospital	26,734,943	
Claims adjustment expenses	776,856	
General administrative expenses	1,856,970	(8)
Total underwriting deductions	29,368,769	
Total underwriting gain or (loss)	(2,317,592)	
Net investment income earned	162,556	
Net investment gains or (losses)	162,556	
Miscellaneous income	13,667	
Net income or (loss) before federal income taxes	(2,141,369)	
Federal and foreign income taxes incurred	(691,800)	
Net income (loss)	$ (1,449,569)	

MOLINA HEALTHCARE OF UTAH, INC.
RECONCILIATION OF CAPITAL AND SURPLUS
1998 through 2001

	1998	1999	2000	Per Exam 2001	Notes
Capital and surplus prior reporting year	$1,027,005	$ 1,171,076	$ 1,054,936	$ 1,177,644	
Increase (decrease in common stock)	99,000				
Increase (decrease) in contributed capital	(87,000)	$ (500,000)			
Net income or (loss)	300,240	430,525	63,337	(1,449,569)	(1) (8)
Change in nonadmitted assets	(168,170)	(46,665)	59,371	(111,868)	(1) (2) (3) (4) (5)
Surplus adjustments: Paid in				3,700,000	
Rounding	1				
Net change in capital and surplus	144,071	(116,140)	122,708	2,138,563	(10)
Capital and surplus end of reporting year	$1,171,076	$ 1,054,936	$ 1,177,644	$ 3,316,207	

NOTES TO FINANCIAL STATEMENTS

(1) Accident and health premiums due and unpaid $1,208,888

As of December 31, 2001, the Organization reported premiums due and unpaid of $1,261,668. The capitation receivable balance was increased by $39,000 to reflect additional receivables determined by the examination. Pursuant to Statements of Statutory Accounting Principles (SSAP) No. 6(9)(a), the examination decreased the receivable by $91,780 due to premiums determined to be uncollectible, which did not qualify as allowable assets.

(2) Amounts recoverable from reinsurers $739,585

The amount reported as recoverable from reinsurers, $763,005, was reduced by $23,420 for examination purposes to reflect an amount that was not confirmed by the assuming reinsurer upon the examination's request. Pursuant to SSAP No. 61(41), uncollectible reinsurance balances shall be written off.

(3) Amounts due from parent, subsidiaries and affiliates $202,168

The Organization reported $1,116,669 as Amounts due from parents, subsidiaries and affiliates as of December 31, 2001. The examination reclassified $955,474 to Federal and foreign income tax recoverable to be consistent with the NAIC *Annual Statement Instructions.*

The Organization offset a payable to an affiliate of $40,973, against the amounts due from its parent and another affiliate of $1,157,642. According to the SSAP No. 64, the Organization does not have the right to offset a receivable and a payable with two separate affiliates. The examination reclassified this payable to Amounts due to parent, subsidiaries and affiliates.

(4) Federal and foreign income tax recoverable and interest thereon $955,474

As noted in number (3), the examination reclassified $955,474 from Amounts due from parents, subsidiaries and affiliates to be consistent with the NAIC *Annual Statement Instructions*. Within ninety days subsequent to the balance sheet date, the Organization collected the income taxes recoverable from its parent, which was consistent with SSAP No. 10(13).

(5) Rent receivable $ 0

The rent receivable of $800, reported in the 2001 annual statement was not recognized for examination purposes, because it was not an admitted asset pursuant to SSAP No. 4(3).

(6) Claims unpaid $6,202,707

The reported amount, $6,393,219, was decreased by $190,512. This amount was reclassified to Unpaid claims adjustment expenses to comply with the NAIC *Annual Statement Instructions*.

(7) Unpaid claims adjustment expenses $190,512

Unpaid claims adjustment expenses increased by $190,512, to reflect the reclassification from Claims unpaid according to the NAIC *Annual Statement Instructions.*

(8) General expenses due or accrued $262,927

The amount reported, $294,927, was decreased by $32,000, to adjust for bonuses that were over accrued.

(9) Amounts due to parent, subsidiaries and affiliates $40,973

The examination reclassified $40,973, from Amounts due from parents, subsidiaries and affiliates in accordance with the SSAP No. 64.

(10) Capital and surplus $3,316,207

The Organization's capital and surplus was determined to be $45,000 less than reported in the Organization's annual statement as of December 31, 2001. The following schedule identifies the examination changes:

Description	Annual Statement Dr (Cr)	Per Examination	Change in Surplus Inc. (Dec.)	Notes
Accident and health premiums due and unpaid	$ 1,261,668	$ 1,208,888	$ (52,780)	(1)
Amounts recoverable from reinsurers	763,005	739,585	(23,420)	(2)
Amounts due from parents, subsidiaries and affiliates	1,116,669	202,168	(914,501)	(3)
Federal and foreign income tax recoverable	-	955,474	955,474	(4)
Rent receivable	800	-	(800)	(5)
Claims unpaid	(6,393,219)	(6,202,707)	190,512	(6)
Unpaid claims adjustment expenses	-	(190,512)	(190,512)	(7)
General expenses due or accrued	(294,927)	(262,927)	32,000	(8)
Amounts due to parent, subsidiaries and affiliates	-	(40,973)	(40,973)	(9)
Total examination changes			(45,000)	
Total capital and surplus per Organization			3,361,207	(10)
Total capital and surplus per examination			$ 3,316,207	

The Organization's minimum capital requirement was $100,000 as defined in U.C.A. § 31A-8-209. As defined by U.C.A. § 31A-17 Part 6, the Organization had total adjusted capital of $3,316,207, which exceeded the company action level risk-based

capital (RBC) requirement of $3,230,978 by $85,229. On December 13, 2001, the board of directors for Molina Healthcare, Inc. approved a capital contribution of $5,000,000, to its subsidiary, the Organization, to meet the RBC requirement.

SUMMARY OF EXAMINATION FINDINGS

Items of significance commented on in this report are summarized below:

1. The Organization made an extraordinary dividend distribution of $500,000 to its parent in the last quarter of 1999. The Organization did not comply with U.C.A. § 31A-16-106(2)(a), because the Organization filed the Form D Prior Notice of a Transaction with the Commissioner until July 31, 2000. (Dividends to Stockholders)

2. The Commissioner was not notified immediately after the election of one director and two principal officers during the examination period. It is recommended the Organization notify the Commissioner immediately after the election of directors and principal officers to comply with U.C.A. § 31A-5-410(1)(a). (Management)

3. The minutes of the board of directors did not indicate the appointment of members of two of its committees. It is recommended the board of directors adopt by resolution the appointment of all committees pursuant Article II Section G of its bylaws. (Management)

4. The Organization did not obtain conflict of interest disclosure statements from its directors and officers during the examination period. The Organization should obtain and keep a record of conflict of interest disclosures from its directors and officers on an annual basis to comply with Section I of its bylaws. (Management)

5. The minutes of the board of directors did not indicate the approval of investments. The board of directors should keep a record of the approval of investments in its minutes to comply with U.C.A. § 31A-5-407(6). (Management)

6. The Organization entered into a services agreement with its parent, Molina Healthcare, Inc. without notifying the Commissioner 30 days in advance of the transaction. All management agreements, service contracts, and all cost-sharing arrangements are to be submitted to the Commissioner 30 days in advance of the transaction according to U.C.A. § 31A-16-106(1)(b)(iv). (AFFILIATED COMPANIES)

7. Some provider agreements did not contain the provision that the enrollee shall not be held liable to the provider for any sums owed by the Organization in the event the Organization fails to pay for health care services as set forth in the provider agreement. Provider contracts should contain the hold harmless provision required by U.C.A. § 31A-8-407(1). (Provider Contracts)

8. Several financial reporting deficiencies were noted. Pursuant to U.A.C. Rule R590-147-4, the annual statement shall be prepared in accordance with the NAIC *Annual Statement Instructions* in an accurate manner. (ACCOUNTS AND RECORDS)

9. The examination disallowed accident and health premiums due and unpaid of $91,780, which were determined to be not collectible pursuant to SSAP No. 6(9)(a). (NOTES TO FINANCIAL STATEMENTS)

10. One assuming reinsurer did not confirm Amounts recoverable from reinsurers, therefore, $23,420 was determined to be uncollectible and not admitted pursuant to SSAP No. 61(41). (NOTES TO FINANCIAL STATEMENTS)

11. The examination reclassified $955,474 from Amounts due from parents, subsidiaries and affiliates to Federal and foreign income tax recoverable. According to the NAIC *Annual Statement Instructions*, intercompany transactions arising from income tax allocations among companies participating in a consolidated tax return are to be reported on line 19 of the asset page. (NOTES TO FINANCIAL STATEMENTS)

12. Rent receivable of $800 was reported as admitted, which was not identified as allowable under SSAP No. 4(3). (NOTES TO FINANCIAL STATEMENTS)

13. The examination reclassified $40,973 to Amounts due to parent, subsidiaries and affiliates. According to SSAP No. 64, the Organization does not have the right to offset a receivable and a payable with two separate affiliates. (NOTES TO FINANCIAL STATEMENTS)

14. Unpaid claims adjustment expenses of $190,512 were reported on the same line as Claims unpaid. The Organization should separately and properly report the Unpaid claims adjustment expenses on page 3 line 3 of the annual statement per the NAIC *Annual Statement Instructions*. (NOTES TO FINANCIAL STATEMENTS)

15. The examination determined bonuses, reported as part of the General expenses due or accrued line in the annual statement, were over accrued by $32,000. (NOTES TO FINANCIAL STATEMENTS)

16. Total adjusted capital determined by the examination was $3,316,207, or $45,000 less than reported as of December 31, 2001. Total adjusted capital exceeded the company action level RBC requirement of $3,230,978 by $85,229. (NOTES TO FINANCIAL STATEMENTS)

CONCLUSION

Thomas L. Burger, FSA, MAAA, of the actuarial firm of Taylor, Walker & Associates performed the actuarial phases of the examination. In addition, David A. Martinez, CFE, participated in the examination representing the Utah Insurance Department. They join the undersigned in acknowledging the assistance and cooperation extended during the course of the examination by officers, employees, and representatives of the Organization.

Respectfully Submitted,

Colette M. Reddoor, CFE
Utah Insurance Department